

## **Domestic Petroleum Council**

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# **Fax Memo**

**To:** Hugh Hilliard (202) 208 3144  
**From:** Bill Whitsitt  
**Date:** 3/18/99  
**Re:** Conference Call Material

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Hugh-

Hope the attached is helpful.

We may also have some illustrative questions to you, hopefully tomorrow.



# **Suggestions for MMS Regarding Workshops**

## **A. Commitment and Assumptions**

- We assume that MMS will engage in meaningful interaction with industry during the workshops that can lead to resolution of key issues.
- The key issues identified in Section C are inter-related to an extent that requires that they be considered as elements of a package.

## **B. Process and Agenda**

The following are merely suggestions of one way to approach the workshops. We would very much appreciate an opportunity to discuss these or other approaches that could lead to meaningful dialogue.

- The room could be set up in a hollow square large enough for small teams representing MMS, industry and other interested parties to sit on each side with plenty of chairs around perimeter of room for resource group members (experts) from MMS and industry.
- The agenda should provide for:
  - Opening statements from MMS, industry and any other stakeholder present. This is an opportunity to set the tone and define the objectives for the day's efforts.
  - A discussion by MMS of current agency views on the proposed rule – building on items raised in Bob Armstrong's August 31, 1999 letter to Senator Breaux.
  - After opening statements the substantive agenda might begin with a discussion by MMS and industry of the list of topics in section C below in order to facilitate a mutual constructive exchange of views.
  - Provide for breaks to allow workshop teams to caucus with their respective experts as needed.
- A small team will represent industry and include representatives of large and small producers, majors and independents, and companies with interests in onshore and/or offshore production.
- Appropriate industry experts on a variety of issues will accompany the industry team to advise team members on technical matters as appropriate.

- To facilitate meaningful discussions, we request that MMS personnel having expertise in the topics described in Section C be present at the workshops if at all possible.

### **C. Key Issues to be discussed at workshops**

1. **Arm's length transactions:** For arm's length transactions, industry has specific recommendations building on the MMS' announced reversion to the existing definition of "affiliate." These recommendations would tune the definition of "affiliate" to establish clear, workable and appropriate bounds on the universe of arm's length transactions. In addition, industry has specific recommendations for addressing the lessees' need for reasonable regulatory assurance that bona fide arm's length transactions will not be set aside by the MMS at some future date.

*For example: We would explore how the affiliate definition is interwoven and is used in the proposed rule in a broader manner than existing regulations. We would explore drafting language for MMS' options for lessee to choose between downstream tracing or non-arm's length methodology; strong focus on lessee's first sale rather than MMS' inclination to rely on downstream transactions.*

2. **Non-arm's length transactions:** For the situation where no arm's length transaction has occurred and gross proceeds is not available as a measure of value, industry has specific recommendations for other measures that would indicate value while minimizing the problems associated with use of an index like crude oil spot prices. Industry's recommendations build on that portion of the MMS' present proposal applicable to the Rocky Mountain Region.

*For example: Industry's recommendations resolve MMS' perceived problems with comparable sales/purchase as incorporated in current benchmarks, captures lease supply and demand factors (+/-), avoids disputes over differentials between lease and market center and is relied on by states and MMS in RIK programs.*

3. **Adjustments off Downstream Values:** For non-arm's length transactions where other measures might not be practicable, use of an index like crude oil spot prices could be feasible, but only if sufficient adjustments were provided to arrive at a reasonable approximation of the value of production.

*For example: Industry recommendation provides transportation and location/quality differential alternatives to better approximate value at the lease, whether a downstream sale or index method is starting point.*

**4. Binding Determinations:** For all transactions, industry has specific recommendations for including in the regulations an explicit process by which lessees trying to comply with MMS valuation regulations could procure from the MMS binding determinations of value. These recommendations are in line with the Department's own communications and the result would be certainty for industry and the government.

*For example: industry's recommendation would require that any decision would be subject to existing appeals procedures and that such determinations would have no precedent value beyond the factual descriptions underlying the lessee's request.*

**Note:** In each issue area industry's proposed approach places a premium on clarity and certainty, while emphasizing the statutory obligation that royalty be paid on the value of production at the lease. Properly revised, the MMS' valuation regulations can be simpler, easier to administer and lead to substantial cost savings for both industry and government without compromising royalty revenue streams.